BEFORE THE HEARING OFFICER
OF THE TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO

IN THE MATTER OF THE PROTEST OF
SOUTHWEST ABATEMENT, **No. 11-05**
TO ASSESSMENTS ISSUED UNDER
ID NOS. L0778204544; L1315075456; L0241333632;
L1986164096; L0912422272; L1290446208;
L0216704384; and L1961534848

DECISION AND ORDER

A formal hearing on the above-referenced protest was held January 6, 2011, before Dee Dee Hoxie, Hearing Officer. The Taxation and Revenue Department ("Department") was represented by Mr. Peter Breen, Special Assistant Attorney General. Ms. Sylvia Sena, Auditor, also appeared on behalf of the Department. Mr. Robert Strumor, Attorney, appeared for the hearing representing Southwest Abatement ("Taxpayer"). Mr. Tad West, President of Taxpayer, Ms. Kendra Veit, an employee of Taxpayer, Mr. Tim Taylor, accountant for Taxpayer, and Ms. Rene Stapf, forensic auditor and consultant for Taxpayer were present for the hearing. Mr. West and Ms. Stapf testified on behalf of Taxpayer. Ms. Sena testified on behalf of the Department. The Hearing Officer took notice of all documents in the administrative file. Taxpayer #1 and #2 were admitted at the hearing. The parties agreed to waive the 30-day decision deadline. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Taxpayer was engaged in business in New Mexico in 2007 and was required to file and pay monthly gross receipts tax ("GRT").
2. Taxpayer relied on its bookkeeper in 2007 to prepare its monthly GRT reports, to prepare its GRT payments, and to file its reports and make payments to the Department.

3. Mr. West would review the monthly reports prepared by the bookkeeper and would sign the GRT payment checks.

4. The bookkeeper regularly prepared lists of outstanding checks so that Taxpayer would be aware of any checks pending. The bookkeeper also handled all of the mail relating to financial matters.

5. A general office manager was the supervisor of the office employees, including the bookkeeper. However, it is unknown what kind of review or oversight the manager actually engaged in with regard to the bookkeeper.

6. In March 2008 it was discovered that the bookkeeper had made an unauthorized deposit in her personal account from Taxpayer's funds. The bookkeeper's employment was terminated after the unauthorized payment was discovered.

7. Ms. Veit took over bookkeeping for Taxpayer. At some point Ms. Veit received a letter from the Department regarding GRT. Ms. Veit alerted Mr. West.

8. The Department determined that Taxpayer was a non-filer on GRT for several months in 2007.

9. On November 4, 2008, the Department assessed the Taxpayer for GRT, compensating tax, penalty, and interest for the tax periods ending on November 30, 2007; October 31, 2007; September 30, 2007; July 31, 2007; and February 28, 2007.

10. On December 3, 2008, the Department assessed the Taxpayer for GRT, compensating tax, penalty, and interest for the tax periods ending on May 31, 2007; April 30, 2007; and March 31, 2007.

11. On November 24, 2008 and December 30, 2008, Taxpayer filed formal protest letters regarding the assessments of penalty.

12. On August 30, 2010, the Department filed a Request for Hearing asking that the Taxpayer's protests be scheduled for a formal administrative hearing.

13. The hearing was set for November 1, 2010. Taxpayer requested that the hearing date be continued so that it could complete an internal forensic audit. The request was granted and the hearing was reset for January 6, 2011.

14. Taxpayer discovered through its forensic audit that the bookkeeper had embezzled over $100,000 from Taxpayer during her employment.

15. Taxpayer also discovered that the GRT reports that had been prepared for the periods covered by the assessments had not been filed with the Department. Taxpayer also discovered that the checks that were prepared as payments for those reports had never been cashed, even though the bookkeeper had removed them from the list of outstanding checks.

16. Taxpayer argues that it was a victim of fraud by the bookkeeper and should not be liable for penalty because it was not negligent or willful in its failure to pay GRT when it was due. Taxpayer argues that it exercised ordinary business care and reasonably relied on its bookkeeper to file the reports and make payments as she was purporting to do.

DISCUSSION

The issue to be decided is whether the Taxpayer is liable for the penalty assessed for the tax periods ending in November, October, September, July, February, May, April, and March of 2007 due to its failure to file and pay GRT when it was due.

Burden of Proof.

Assessments by the Department are presumed to be correct. *See* NMSA 1978, § 7-1-17. Tax includes, by definition, the amount of tax principal imposed and, unless the context

otherwise requires, "the amount of any interest or civil penalty relating thereto." NMSA 1978, § 7-1-3. *See also El Centro Villa Nursing Center v. Taxation and Revenue Department*, 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989). Therefore, the assessment issued to the Taxpayer is presumed to be correct, and it is the Taxpayer's burden to present evidence and legal argument to show that it is entitled to an abatement of penalty.

Assessment of Penalty.

Penalty is assessed when tax due is not paid on time, even when the non-payment is because of negligence or disregard of rules and regulations. *See* NMSA 1978, § 7-1-69. Penalty is also assessed when failure to pay on time is due to willful intent to evade tax. *See id.* However, willful evasion is not the issue in this case.

Taxpayer argues that it was not negligent and was not in disregard to rules and regulations because it reasonably relied on its employee, the bookkeeper, to file the reports and make tax payments. Taxpayer argues that its practice of having Mr. West review the reports and sign the checks, of having the bookkeeper prepare lists of outstanding checks, and of having a supervisor assigned to the bookkeeper was sufficient to show ordinary business care. Taxpayer argues that it was, therefore, not negligent. The Department argues that the Taxpayer did not have reasonable safeguards in place. The Department argues that the bookkeeper was essentially unsupervised, had unfettered access to the business accounts, and controlled all of the information regarding the accounts and the taxes.

Negligence includes a failure to exercise ordinary business care, inaction when action is required, inadvertence, and erroneous belief or inattention. *See* 3.1.11.10 NMAC (2001). A person who reasonably relies on advice from competent tax counsel or an accountant may be found nonnegligent. *See* 3.1.11.11 (D) NMAC (2001). "[F]ailure to make a timely filing of a tax

return, however, is not excused by the taxpayer's reliance on an agent[.]" *Id.* *See also U.S. v. Boyle*, 469 U.S. 241 (1985) (holding that the taxpayer did not demonstrate ordinary business care when taxpayer failed to file a return even though the taxpayer's failure was caused by reliance on the attorney who had been hired to file the return). A taxpayer is responsible for the filing of the taxpayer's returns, even when they have hired another to do the filing for them. *See El Centro Villa Nursing Center*, 108 N.M. 795 (holding that a taxpayer was negligent for purposes of penalty even though taxpayer had relied on its accountant to properly report and pay its taxes). Therefore, Taxpayer was negligent in relying on its bookkeeper to file its returns, and penalty was properly assessed.

Computation of Penalty.

On all of the assessments issued in this matter, the Department seeks to impose a penalty of up to 20% under NMSA 1978, § 7-1-69 (2008). The assessments were issued for taxes due in 2007. The latest month assessed was November 2007. The tax for that month would have been due in December 2007. *See* NMSA 1978, § 7-9-11. The applicable penalty statute in effect for the 2007 tax periods was capped at a maximum penalty "not to exceed" 10%. *See* NMSA 1978, § 7-1-69 (2003). Ms. Sena testified that the Department had assessed a 20% cap because the tax was assessed after the effective date of the 2008 amendment. Without evidence of legislative intent for retroactive application of NMSA 1978, Section 7-1-69 (2008), the outstanding tax due for tax periods in 2007 were subject to a penalty "not to exceed" 10% pursuant to NMSA 1978, Section 7-1-69 (2003) because that was the provision in effect at the time the tax was due. *See Kewanee Industries, Inc. v. Reese*, 114 N.M. 784, 845 P.2d 1238 (1993) (holding that a modified penalty regulation would not apply retroactively when the regulation was enacted after the applicable tax year).

Interest Accrues Only on Tax Due.

Taxpayer asked that any interest accrued on the amount of penalty be abated. Interest is imposed on the amount of tax due which is not paid when it becomes due. NMSA 1978, § 7-1-67 (A). Interest is not imposed on the amount of interest or on the amount of penalty. NMSA 1978, § 7-1-67 (C). Therefore, interest has not and will not accrue on the amount of penalty.

CONCLUSIONS OF LAW

1. Taxpayer filed timely written protests to the Notices of Assessment issued under Letter ID numbers L0778204544, L1315075456, L0241333632, L1986164096, L0912422272, L1290446208, L0216704384, and L1961534848, and jurisdiction lies over the parties and the subject matter of this protest.

2. The assessment of penalty for the 2007 tax periods was appropriate. However, the computation of penalty was incorrect. Penalty is capped at an amount not to exceed 10%. The amount of any penalty assessed in excess of the 10% cap is hereby abated.

For the foregoing reasons, the Taxpayer's protest **is GRANTED IN PART AND DENIED IN PART**.

DATED: February 9, 2011.